



FmHA AN No. 2492 (1924)
March 12, 1992

SUBJECT: Credit Quality and the Utilization of Credit and
Financial Analysis Worksheets and Techniques on
Insured Farmer Programs Loans

TO: State Directors, District Directors, and County
Supervisors

ATTN: Farmer Programs Chiefs

PURPOSE/INTENDED OUTCOME:

The utilization of the Credit and Financial Analysis Worksheets by field personnel is intended to improve FmHA supervision and, thereby, increase the probability of financial success for insured borrowers. To accomplish this, we must communicate effectively with borrowers, and base any concerns we may have on a credible analysis. The Credit and Financial Analysis Worksheets serve us well by documenting our credit analysis decisions, and helping us to systematically identify the strengths and weaknesses in each borrower's farming operation.

COMPARISON WITH PREVIOUS AN:

This AN replaces AN No. 2368 dated September 23, 1991, which implemented the concepts and analysis techniques introduced at the Credit and Financial Analysis training in St. Louis, Missouri.

This AN is being re-issued in response to the numerous questions from the field indicating that more specific direction is needed. This revised AN (1) expands the guidance on the use of the Credit and Financial Worksheets, (2) clarifies that approval of loan or servicing action will not be delayed in order to complete the worksheets, (3) advises that the National Office will assess the quality of the analyses through the Coordinated Assessment Review (CAR) process, and (4) requires State Coordinators to be appointed to answer field office questions about utilization of the worksheets and administrative requirements discussed herein.

EXPIRATION DATE: February 28, 1993

FILING INSTRUCTIONS:
Preceding FmHA
Instruction 1924-B



Credit and Financial Analysis requirements will be fully incorporated in regulations being written to comply with 1990 Food, Agricultural, Conservation and Trade (FACT) Act requirements for Loan Assessments (Farm Business Planning).

IMPLEMENTATION RESPONSIBILITIES:

The 1990 FACT Act directed FmHA to train its employees on Credit and Financial Analysis and Farm Management to ensure adequate and effective supervision of farm borrowers. The training in Credit and Financial Analysis was designed to begin the process of meeting the Congressional mandates.

We must now proceed toward this objective through (1) the identification, analysis and documentation of the specific financial strengths and weaknesses of each farming operation, and (2) effective communication with borrowers to ensure that specific financial management practices necessary to reverse adverse trends are addressed as part of the Key Management Practices on Form FmHA 431-2, "Farm and Home Plan," and in loan conditions set forth on Form FmHA 1940-1, "Request for Obligation of Funds."

Analysis Process

In all cases where FmHA receives a loan application, or request for subordination or debt restructuring under FmHA Instruction 1951-S, an analysis must be performed and documented by applying the techniques introduced at the training sessions, and using the appropriate Capital Management, Historical Performance, and Annual Performance Evaluation Worksheets as discussed later in this AN. The analysis required by this AN does not apply to any borrower being serviced for the express purpose of liquidation through debt settlement.

Ideally, these worksheets should be completed prior to approval of the loan or the servicing action. However, loan making or servicing decisions will not be delayed for the sole purpose of completing the worksheets. Therefore, on or prior to January 1, 1993, the worksheets can be completed on a post-approval basis. Once the automated worksheets are released, however, it is strongly suggested that the worksheets be completed prior to approval. The permitted delay in completing the worksheets is temporary, pending automation. This does not alleviate the need for a thorough loan analysis prior to approval of each case. Any actions after January 1, 1993, will require completion of the worksheets and analysis prior to approval.

The most valid trend analysis is achieved when financial statement dates are as of the same date each year. The more varied the dates, the less reliable the findings will be from your analysis. However, you may be faced with less than ideal information when you complete the worksheets, and you must take this into account as you develop the conclusions of your analysis.

Beginning farmers and other first-time borrowers may not have complete financial data, and you will have to use the best data you can obtain to perform the trend analysis. If the borrower does not have a current balance sheet, assist them in preparing one. If the borrower has been doing business with other lenders, they are a likely source of financial information. The loan file must always be documented to justify any case using less than the required information.

Worksheet Guidelines

For FY 1992, you will need to make copies of the worksheets distributed at the training session. The running case record should clearly address the issues identified and then set forth proposed resolutions to which you and the borrower have agreed.

A well-documented case file is a fundamental element in the lending process. The FMHA official should always verify and document prices, yields, expenses, debts, borrower financial trends, operational changes, etc. Thorough documentation of the loan decision process leaves no doubt as to the basis for any action taken. Extraneous information, such as multiple or incomplete cash-flow budgets, should not be kept in the loan file. If multiple budgets are required (i.e., typical plan and projected plan), each document should be clearly marked.

Preliminary analysis will consist of completion and analysis of (1) Historical Performance Worksheet; (2) Capital Management Worksheet - Required Cash Profit section only; and (3) Annual Performance Worksheet - Decision and Annual Performance sections only.

As a result of the above preliminary analysis, there are four possible conclusions:

1. The operation is sound with no apparent production or capital problems or significant changes.
2. The production efficiency of the operation is above average (greater than 30%), but there is a capital problem.
3. There is no capital problem, but the production efficiency of the operation is average or below (less than or equal to 30%).
4. The operation has both production and capital problems or the operation is a new producer.

The attached table offers guidelines for completing the worksheets as part of a loan analysis for each situation. Your analysis will include, but should not be limited to, the minimum requirements suggested. Some key situations are described but any area of concern should be addressed with further analysis as necessary. In each case, the appropriate sections of the

worksheets will be completed with accurate information and analyzed, and loan decisions based on this analysis will be properly documented in the case file.

Support and Oversight

The quality of the credit and financial analyses will be reviewed through the Coordinated Assessment Review process.

Each State Director should appoint an individual to serve as coordinator for all questions relating to the proper use of the Worksheets and any other requirements of this AN. This State Coordinator should be the same individual who is serving as Farm and Home Plan Coordinator if possible.

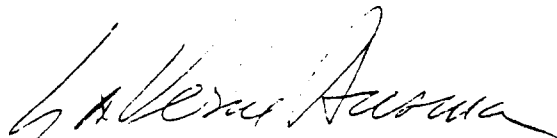
The National Office Coordinator is Steven Rubin, Farmer Programs, Program Development Staff. Questions from State Coordinators should be directed to him at (202) 690-4003. The name, title and phone number of the State Coordinator must be telemailed (no.pds) or faxed (202 or FTS 720-8474) to Steven Rubin within 20 working days of the date of this AN.

General Guidance

As high risk credit experts experienced in working with distressed financial situations, you are in the unique position to assist borrowers in identifying negative trends before they become so serious as to threaten failure of the borrower's operation. Therefore, in carrying out an effective supervised credit program, you will need to discuss the results of your analysis with each borrower and set forth the action plan necessary to reverse the negative trends. If the trends are irreversible, the borrower must be counselled concerning the high probability and consequences of failure. The borrower must also be advised that the Agency may be unable to provide future credit when trends are irreversible.

Intensifying our supervised credit role is an immediate need. Additional tools, especially in the automation area, are being developed and will be provided as rapidly as they can be completed and tested.

Any revisions or modifications to this AN that you wish to publish as State directives must be submitted and approved by the Assistant Administrator, Farmer Programs, before they are released for implementation in your State.



LA VERNE AUSMAN
Administrator

Attachment - Worksheet Guidelines

CREDIT AND FINANCIAL ANALYSIS WORKSHEET GUIDELINES

HISTORICAL
PERFORMANCE

CAPITAL MANAGEMENT WORKSHEET

ANNUAL
PERFORMANCE

	ALL SECTIONS	CAPITAL MANAGEMENT WORKSHEET										ANNUAL PERFORMANCE			
		PAGE 1		PAGE 2		PAGE 3				PAGE 4		PG 1-1	PG 2-1	PG 3-1	PG 4-1
		DECISION	ASSET ANALYSIS	CREDIT LIMIT RULE	LIQUIDITY TEST	REQUIRED CASH PROFIT	DEBT RESTRUC- TURING	RESTRUC- TURED DEBT	ADDTL DEBT/ EXPANSN	STRUCTURE AFTER EXPANSN	ASSET ANALYSIS STRUCTURE	DECISION	ANNUAL PERFORM.	INCOME ANALYSIS	KEY EXPENSE ANALYSIS
1. ALL CASES:	X					X						X	X		
2. THEN LOOK FOR THE FOLLOWING:															
SIGNIFICANT CHANGES HAVE OCCURRED IN OPERATION	X	X	X	X	X	X					X	X	X	X	X
NEW OPERATION	X	X	X	X	X	X					X	X	X	X	X
LESS THAN 5 YEARS DATA AVAILABLE	X		X	X	X	X						X	X	X	X
PRODUCTION EFFICIENCY IS BELOW AVERAGE (OP. PROFIT MARG. < 30%) (REF. LINE 3a OF HPW)	X					X						X	X	X	X
FLUCTUATION IN HISTORICAL OPERATING EFFICIENCY (REF. LINE 3A OF HPW)	X					X						X	X	X	X
CAPITAL PROBLEMS (INCLUDING THE FOLLOWING:)	X	X	X	X	X	X	X	X			X	X	X		
REQUIRED CASH PROFIT SHOWS SHORTFALL ANY OF NEXT 5 YRS	X	X	X	X	X	X	X	X			X	X	X	X	X
ADDITIONAL DEBT PLANNED	X	X		X	X	X			X	X		X	X		
REVENUE/ASSET RATIO LESS THAN 0.2:1.0 (REF. LINE 16 HPW)	X	X	X	X		X					X	X	X	X	X
EARNED EQUITY LESS THAN OR EQUAL TO ZERO (REF. LINE 7 HPW)	X	X	X	X	X	X						X	X		
DEBT INCREASING OVER TIME (REF. LINE 8 HPW)	X	X	X	X	X	X					X	X	X	X	X
PRINCIPAL + INTEREST IS GREATER THAN 50% OF PROFIT (LINE 14 + LINE 4 > 50% OF LINE 3)	X	X	X	X		X					X	X	X		
CURRENT RATIO IS LESS THAN 1:1 (REF. LINE 10 HPW)	X	X	X		X	X	X	X			X	X	X		
DECLINE IN WORKING CAPITAL (REF. LINE 12 HPW)	X	X	X		X	X	X	X			X	X	X		

NOTE:

COMB. / APPROPRIATE SECTIONS OF WORKSHEET FOR EACH APPLICABLE SITUATION FOR THIS OPERATION.
 "P.W. L." INDICATES THE LINE ON THE HISTORICAL PERFORMANCE WORKSHEET WHERE THE INFORMATION IS FOUND.